



Human Capital Management

AN ANALYSIS OF DISCLOSURE IN UK REPORTS



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Background

In 2004, to provide a little more context to specific reporting areas, the *ACCA UK Awards for Sustainability Reporting* introduced annual themes to run alongside the main analysis, in partnership with an organisation specialised in the chosen topic. The theme in 2004 was Stakeholder Engagement, run in partnership with the Environment Council, 2005 was Bribery and Corruption with Transparency International, 2006 was Climate Change with FTSE Group, 2007 was Strategy and Governance with Tomorrow's Company, and 2008 Human Capital Management (HCM) with the Chartered Institute of Personnel and Development (CIPD). This report presents the results of the HCM disclosure analysis.

Introduction

Over the last ten years, the issue of human capital and its contribution to business success has risen up the management agenda. It is now generally considered that many business opportunities can be found in a firm's intangible assets, which include intellectual capital and a diverse, knowledgeable and skilled workforce. Conversely, it is also widely believed that poor management of human capital is one of the most significant risks facing organisations, as demonstrated by a survey of CEOs carried out by *McKinsey Quarterly*.¹ The results identified talent constraints, poor public governance and climate change as the most critical issues for organisations to address. Organisations are striving to find better ways of understanding and reporting on the value of people to business and the part that human capital plays in sustainable future success. Issues that management should be, and are, starting to consider in their disclosures are:

- the inclusion of HCM in the development of business strategy and objective setting
- consideration of areas such as: diversity, training and development, equal opportunities and positive leadership
- employee health and safety, and well-being and absenteeism
- attraction and retention of the workforce, and turnover rates.

In 2003, the UK government recognised the lack of human capital information in company reporting and set up the Accounting for People Task Force.² Its aims were to look at the performance measures used to assess human capital and consider best practice in human capital reporting and the performance measures that are most helpful to stakeholders. The resulting report defined HCM as 'an approach to people management that focuses on the issues that are critical to the organisation's success'. It treats people management 'as a high-level strategic issue and seeks systematically to analyse, measure and evaluate how people policies and practices create value'. It went on to make a number of recommendations, including that reports on HCM should have a strategic focus and communicate 'clearly, fairly and unambiguously the Board's current understanding of the links between the HCM policies and practices, its business strategy and its performance'.

Professor Harry Scarborough and Juanita Elias, reporting on human capital for the Chartered Institute of Personnel and Development in 2002,³ noted that the most useful contribution of human capital to date is in defining the link between HR and business strategy, which is one of the criteria focused on in this report. Much of the subsequent work funded and carried out by the CIPD has been driven by the need to feed human capital information into the strategy formulation process. Indeed, a human capital approach implies that a realistic business strategy must be informed by human capital data. In other words, how can a business pursue a strategy that does not take account of the capacity of all the resources available, including intellectual capital and a skilled workforce?

1. Debby Bielak, Sheila M. J. Bonini, and Jeremy M. Oppenheim 'CEOs on Strategy and Social Issues', *McKinsey Quarterly*, October 2007.

2. Accounting for People Task Force, *Accounting for People*, DTI, 2003.

3. Scarborough, H. and Elias, J., *Evaluating Human Capital*, CIPD, 2002.

A number of factors, therefore, have therefore fed the thirst for more human capital information. In 2003 the Accounting for People Task Force concluded that:

'...greater transparency on how value is created through effective people policies and practices will benefit organisations and their stakeholders.

HCM reporting is highly relevant to institutional investors who manage investments on behalf of beneficiaries: the concept of 'responsible ownership' certainly suggests that investors should take a greater interest in the sustainability of the organisations they help to fund.'

CURRENT REQUIREMENTS

There are currently few mandatory requirements for businesses to report on HCM in the UK. The Business Review element of the updated Companies Act (passed in November 2006) includes reporting on non-financial issues, such as the environment, employees and the community, but leaves it to directors' discretion to report on those issues deemed material to organisational performance. It does, however, impose a legislative duty on directors to consider employees in their decision making.

In terms of investor demand for HCM information, the situation is not clear cut. The findings of some research and projects, one of which is the Accounting for People taskforce outlined above, found that investors do require detailed HCM data and information when making decisions and analyses. Nonetheless, the current HCM information available to investors is not believed to be at a standard where they can usefully incorporate it into analysis and decision making. A piece of research carried out by the CIPD backed up this assertion, and found that although investors value any information that enhances understanding of how a business works and organisational performance, the current level of disclosures does not

assist investors to make better-informed judgements about long-term economic performance.⁴

Another piece of research by the Chartered Management Institute⁵ concluded the following.

'Amongst investors a self-fulfilling prophecy appears to be at work. Investors currently take little account of workforce metrics because there is little or no evidence of comparability, consistency of predictability in their presentation. Yet the investors we interviewed believed that if HCM metrics were delivered on a dependable basis, they would be valuable when assessing organisational performance.'

To date most of the work on human capital reporting has focused on the area of financial reporting and, therefore, has expressed the value of people as a ratio of the total value of the business. This approach is slowly changing, and there is an increasing realisation that HCM is a sustainability issue, as well as a business issue, which should be reported on accordingly in both the stand-alone sustainability report and the annual report/business review. Investors and other stakeholders who read reports (including employees) require transparent, detailed information on organisational human capital strategy and performance to get a clear idea of how both the intangible and tangible elements of a business are considered when making business decisions.

4. *Research Insight: Investor's Views of Human Capital*, CIPD, 2007.

5. Scott-Jackson, W., Cook, P. and Tajar, R., *Measures of Workforce Capability for Future Performance*, Chartered Management Institute, 2006.

Research methodology

The 2008 ACCA Sustainability Reporting Awards theme research was based on an analysis of 40 entrants' reports. These 40 organisations were selected randomly and were deemed to be a large enough sample to gain an idea of the standard of the HCM reporting of UK organisations (see Table 1).

The criteria used in the research were developed jointly by ACCA and the CIPD, using various existing reporting criteria and in-house expertise. The resulting criteria can be seen in Table 2, and drew on the G3 Sustainability Reporting Guidelines, the UN Global Compact and a similar piece of research carried out by ACCA Australia, in partnership with Net Balance Foundation.⁶ All 40 reports were assessed using these criteria by the CIPD and had a secondary detailed check by both an ACCA representative and an independent researcher. The criteria were split into three key groups: strategic intent; governance and assurance; and policy and performance. The percentage score in each group of criteria was worked out by calculating the percentage of the total possible number of points for that group. This technique was also used to calculate the overall percentage scores.

Table 1: List of organisations included in the analysis

Anglo American plc	Home Retail Group plc
Arcelor Mittal	Island Waste Services
Associated British Ports Holdings Ltd	John Lewis Partnership
Aviva plc	Kingfisher plc
AWE plc	Legal & General Group plc
BAA Ltd	J Sainsbury plc
Barclays plc	Segro
BHP Billiton plc	Royal Dutch Shell plc
BG Group plc	Solutia UK Ltd
BP Exploration	Standard Chartered Bank
British American Tobacco plc	Taylor Wimpey plc
BT Group plc	Tesco plc
Camelot Group plc	Traidcraft
Cattles plc	Tullow Oil plc
Co-operative Group Ltd	Unilever plc
Croda International plc	Upstream
The Crown Estate	Vodafone Group plc
EON UK plc	Wates Group
Go Ahead Group	Workspace Group
The Guardian	Xstrata plc

6. ACCA and Net Balance Foundation, *Reporting Trilogy: Research on Sustainability Reporting in Australia: Part 3 – Reporting on Human Capital Management*, ACCA, 2008.

Table 2: Overview of groups of criteria

Strategic intent	
Strategy	Description of the link between HCM and business strategy and evidence of employee input into development of business direction
Materiality	Identification of material HCM issues for inclusion in strategy, and evidence of execution of strategy
Vision	Disclosure of organisational vision and values and how they are disseminated.
Engagement	Evidence of robust employee engagement on future business direction, strategic planning and decision making.
Governance and assurance	
Governance	Evidence of robust governance structures in place to manage HCM performance, including board committees, individual board member responsibility and remuneration linkages to HCM performance indicators
Assurance	HCM information is assured using the AA1000AS and/or ISAE3000 standards
Policy and performance	
Performance	Systematic reporting on material HCM performance areas, including KPI data and narrative information and SMART targets
Policy	Description of any policies and management systems in place to manage key HCM performance areas

The information assessed against these criteria was that contained in the reports submitted for the ACCA Sustainability Reporting Awards 2008, including any online reports or annual reports. Where an organisation was not scored for a particular criterion, this does not necessarily mean that this issue was not addressed and/or measured internally, just that information on the issue was not disclosed in the information assessed.

The findings

OVERALL

Some key findings immediately emerged from the analysis of the results of the assessment. All but two of the reports assessed included a section on their employees and apparently viewed them as a key stakeholder group in sustainability. Many included informative case studies to highlight specific examples of the contribution of people and many wove the people aspects of their business into all aspects of sustainability. For example, Standard Chartered Bank's goals for 2007 included the following.

Embed sustainable lending training in core risk management training.

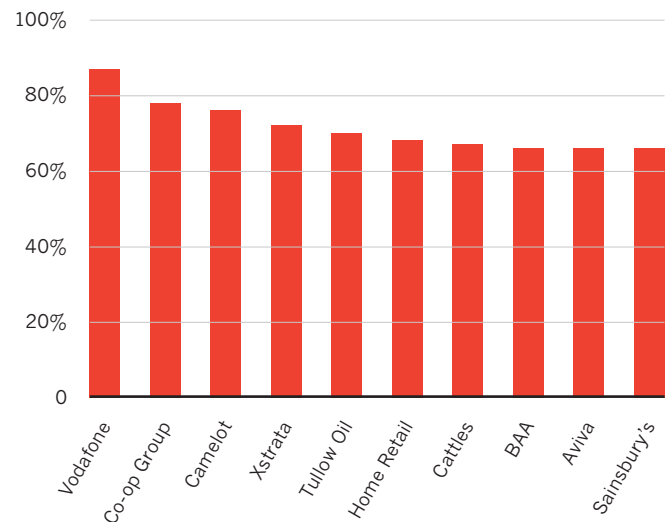
Review our approach to climate risk, including raising levels of awareness amongst appropriate staff on how to assess climate risk.

Upgrade the social, ethical and environmental (SEE) e-learning. Get external stakeholders' input.

Nonetheless, as for other ACCA studies of this type, including the one carried out by ACCA Australia and Net Balance Foundation, the overall standard of the 40 organisations assessed was lower than hoped, with an average overall score of 49% (compared to 28% in the Australian study, assessing the ASX 50). Given that it has been widely publicised for the last few years that HCM reporting is an important element of developing strategy and objective setting, this was disappointing. Yet the top ten organisations scored an average of 72%. The highest scoring company, Vodafone, achieved 87% (see Fig. 1), which could be taken as a positive sign that some organisations have made significant advances.

It was equally encouraging that many of the CEO statements or report introductions mentioned people and the role they play in driving sustainability. In addition, there were a few 'exemplars' who wove metrics and evidence throughout their reports, proving the integral role of people in driving both sustainability and organisational performance.

Figure 1: Top 10 performing organisations overall across all HCM criteria



STRATEGIC INTENT

This group of criteria was concerned with disclosures on HCM strategy setting; key and material HCM issues for the business; evidence of engagement with employees on material issues; and the disclosure of organisational vision and values.

The overall score of the 40 organisations in this criteria group was 54% – which was the highest scoring of the three criteria groups, indicating that organisations are disclosing more about their HCM strategies, material issues and vision and values statement than about governance and actual HCM performance. Those organisations that are not disclosing information on these issues leave readers unclear as to how much of a priority employees and human capital are to business strategy and performance. The top ten scoring organisations had an average score of 74%, with Vodafone leading with 94%, followed by Sainsbury's with 89% (see Fig. 2).

43% of the 40 organisations state in their disclosures that HCM is integral to core business strategy and the future of the business, as well as describing the stand-alone strategic approach to HCM. For example, Vodafone, in their report, made it clear that employees are a very important element of achieving their business goals.

'A key challenge in a company of approximately 71,000 employees is to embed CR at every level in every local operating company. Achieving this means communicating with employees and creating an organisational culture where the instinctive course of action is the responsible course of action, based on our Business Principles... We rely on our people – their enthusiasm, their talent, their commitment – to maintain and build on the success of our business, even more so in today's competitive market. We depend on our people to deliver excellent service to our customers.'

Figure 2: Top 10 performing organisations in the strategic intent group of criteria

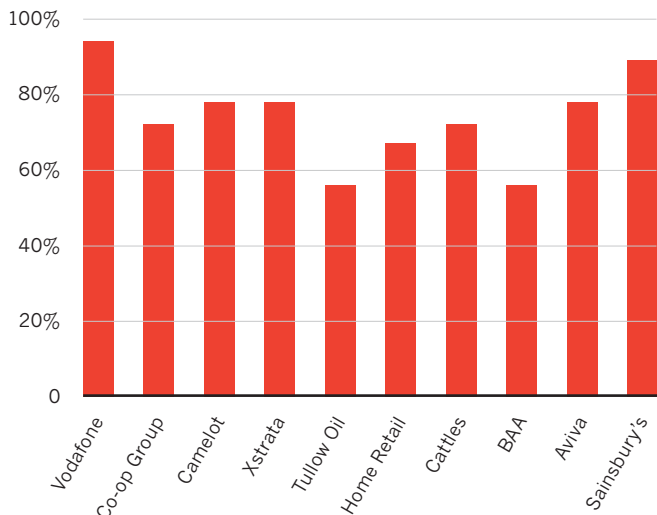
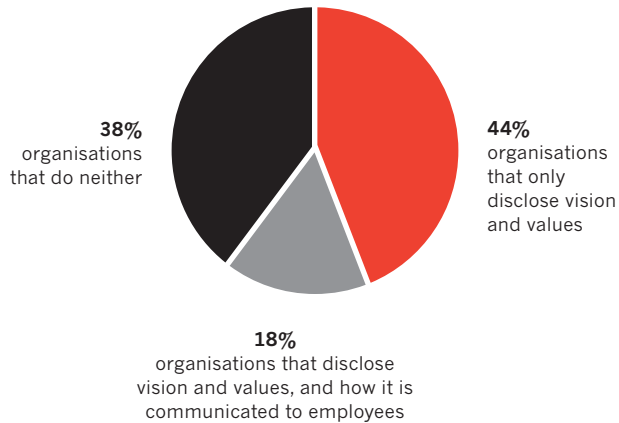


Figure 3: Percentage of organisations disclosing their vision and values



Less encouragingly, 43% of organisations did not mention in their reporting any form of engagement with employees via surveys, focus groups and so on, for inputting into organisational decision-making processes. Of those that did state that these methods of dialogue took place, only 35% gave detailed feedback of the results of any such dialogue. These were BAA, Camelot, EON, The Guardian, Sainsbury's and Vodafone.

Of the 40 organisations, 63% disclosed their organisational vision and values, and of that 63%, 28% explained how they are communicated to all employees (see Fig. 3). For example, Aviva gave the following explanation in their report:

'Values: Our principles of good business ethics are communicated to employees in various ways, ranging from inclusion in induction programmes and management training courses, to our business in Canada seeking annual acknowledgement from all employees that they understand and accept the business' code of conduct.'

GOVERNANCE AND ASSURANCE

This group of criteria related to evidence in the organisation's report as to whether there was a robust governance structure in place to manage HCM and sustainability issues – including board responsibility for HCM, remuneration linked to sustainability, and a whistle-blowing process for grievances to be aired. The assessors also looked for external assurance of the HCM data contained in the report (in accordance with AA1000AS and/or ISAE3000).

The average score of all 40 organisations was 47%, with the top ten organisations scoring an average of 72%. Aviva and the Co-op Group led the group with a top score of 100% (see Fig. 4).

Of the 40 organisations, 58% made clear in their reports that HCM and sustainability are the board's responsibility, either by having a specific board member in charge of the topic or a statement expressing general overall board responsibility. 68% had a board level committee which dealt either specifically with HCM issues, or with overall sustainability performance management, which was expressed elsewhere as including HCM. 25% stated that remuneration policies were linked in some way to HCM or sustainability performance (see Fig. 5).

Figure 4: Top 10 performing organisations in the governance and assurance group of criteria

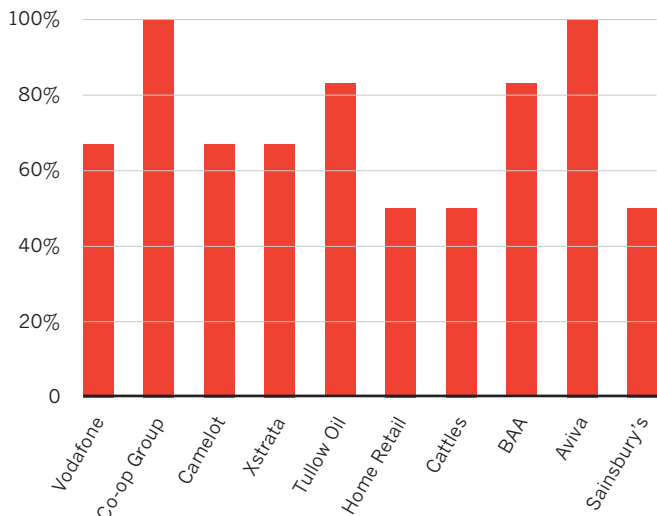
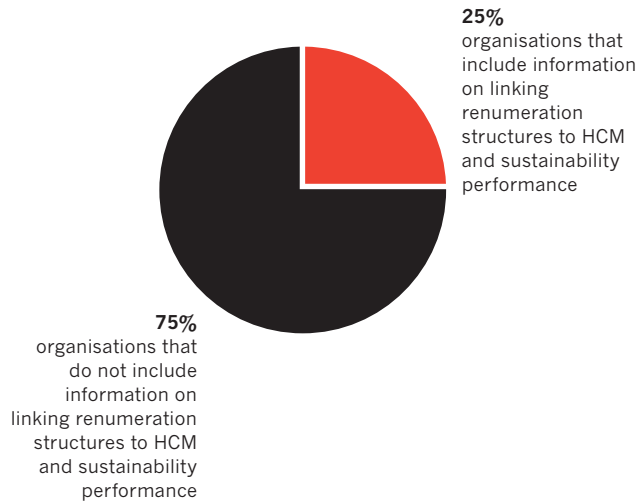


Figure 5: Percentage of organisations that refer to remuneration policies in their reports



The Co-op Group was one of ten organisations that demonstrated linking HCM related issues into remuneration policies. They stated that improvement targets for the employee engagement index, carried out each year, were linked into the performance management process for senior managers. Similarly, Aviva's senior management performance measures were linked to the results of their employee satisfaction survey.

Just under half of the organisations' reports were assured using the AA1000AS or ISAE3000 standards. There were a couple of others who had external assurance statements in their reports, but the assurance provider did not use either of these standards as a guide so were not awarded the point. ACCA advocates the use of the AA1000AS and ISAE3000 in assurance, to ensure that the process is as credible, transparent and comparable as possible.

Policy and performance

This group of criteria related to evidence that performance in material HCM areas was both managed (by policy implementation, target setting, etc) and measured in terms of key performance indicators and narrative disclosures. The assessors looked at the HCM issues considered material for all organisations, including: health and safety, diversity, equal opportunities, employee development and training, employee volunteering and reward/retention.

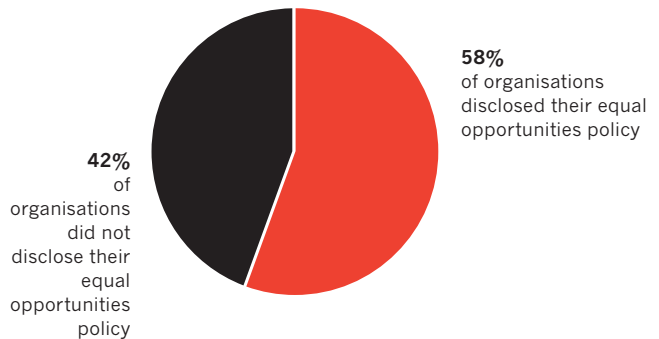
The overall average score for all organisations for this group of criteria was 48%, with a Top 10 average of 71%. Vodafone led with a score of 89%, followed by the Co-op Group with 76%.

Of all the different performance areas assessed, those most frequently mentioned were: the disclosure of an equal opportunities policy (33% of organisations), a detailed description of the health and safety management system in place (53%), employee injury rates (68%), a description of training and development programmes for employees (73%), and target setting for material HCM performance indicators (70%).

There were a number of examples of good reporting in these areas. Among them was Aviva's comment on training, which included several references to its commitment to employee development and how it was linked to strategic priorities.

'We want to create an environment where all our people are encouraged and supported to develop their skills, give of their best and achieve their full potential, as well as to maximise productivity and fulfil our business objectives. Therefore, managing our employee talent is fundamental to our success.'

Figure 6: Percentage of organisations that disclosed their equal opportunities policy



In terms of reporting on health and safety management, Anglo American's report set out its vision for health and safety.

'Our vision is to achieve zero harm and a healthy and productive workforce through the effective management of occupational health risks in all our managed operations. We believe our people are our key asset and we do not accept that it is necessary for people to be made ill whilst working for us. All employees should be able to return home fit and well at the end of each shift.'

This statement was backed up with detailed information on employee injury rates and training and the employee assistance/well-being programmes in place.

Xstrata's statement on development of employees demonstrates that they take career development and training seriously, with the aim of recruiting and retaining high-calibre staff.

'We aim to attract and retain the best people at every level of our businesses and to provide them with the resources they require to achieve and maintain our operational excellence. We provide industry-leading career development opportunities, well structured employment contracts and fair and competitive remuneration.'

Just 18% of the organisations included a figure for the number of disabled people in the workforce, and 30% described in detail the performance management programmes in place for employees to progress in their careers (performance reviews, etc). Both these are fundamental elements of HCM that all organisations should be addressing and including in reports to stakeholders. Finally, despite the growing recognition of the value of retaining talent, only 43% reported on retention or staff turnover figures.

Conclusion

It was immediately clear from the sample assessment that many organisations view their employees as an important factor in their drive for sustainability. It was encouraging that the top ten performing organisations scored 72%, with Vodafone coming first with 87%. Nonetheless, the overall average percentage score of 49% (of all organisations assessed) demonstrates significant room for improvement. All but two of the organisations assessed included a section on ‘people’ or ‘employees’ in their reports and demonstrated that employees were considered a key stakeholder. Many of the CEO statements or introductions to the reports also mentioned people and the role they play in driving sustainability.

Of all the criteria reported upon, the group on which organisations scored highest was strategic intent, with an average of 54% (top ten – 74%). This indicates that organisations may find it easier to report on their strategies for managing human capital issues and vision and values, than on governance or actual performance in the different areas.

The reporting criteria covering governance and assurance achieved an average score of 47% (top ten – 72%). Just under half the organisations had their reports assured using the AA1000AS or ISAE3000 and just over half made clear that HCM and sustainability were dealt with at board level.

The criteria relating to reporting on organisational policy and performance achieved an average score of 48% (71% for the top ten organisations). Some performance areas, such as diversity, health and safety management and training and development, were reported more comprehensively than others, and there was a surprising lack of reporting on factors such as employee retention and the employment of disabled workers.

The research’s findings indicate that headline statements were not always backed up by hard evidence or commentary. Nonetheless, there appeared to be a reasonable level of understanding, particularly among the higher-scoring entries, of the contribution an organisation’s people make to sustainability.

Recommendations for improvement

This study, although carried out on a small sample of reports, indicates that there is still some way to go in terms of disclosing detailed, transparent and credible information on HCM performance. As a result of the research, ACCA and the CIPD make the following recommendations for organisations to take on board when working on future sustainability reports.

STRATEGIC INTENT

An organisation's report should make clear the link between business strategy and HCM issues. Employees are a key organisational stakeholder and factor in achieving operational targets, so should be prioritised when setting strategic objectives.

Organisational vision and values should be disclosed, demonstrating how the organisation has strived for a responsible company 'ethos' that all employees should be following. Dissemination methods should also be disclosed, demonstrating employee education on organisational values.

Reports should also make clear what the organisation is doing to drive employee engagement and what this means for future business strategy and targets – via a description of the methods used (engagement surveys, employee attitude surveys, measure of satisfaction and contentment, focus groups, etc) and the actions taken as a result of employee feedback.

GOVERNANCE AND ASSURANCE

The governance structures in place to manage HCM issues are also an important disclosure area. Reports should outline in detail how HCM is managed throughout the whole organisation, via board committees, individual board member responsibility, senior management structures, etc.

Board level and senior management remuneration should also be linked in some way to HCM target setting, and a statement of this should be included in reporting.

HCM information (along with other sustainability data) should be assured using either the AA1000AS or ISAE3000, or both. Assurance makes information more credible for the reader and helps highlight any omissions and gaps in the report that can be addressed in future years.

POLICY AND PERFORMANCE

Material HCM issues for the organisation should be clearly identified in the report, along with a description of the process used to identify these issues. A discussion of why these are important together with an analysis of the risks should be included.

As well as a narrative description of each issue, KPI data, targets and any policy statements should also be disclosed. Targets should be 'SMART' (Specific, Measurable, Achievable, Relevant and Timely) and developed in consultation with stakeholders, including employees.

About ACCA

ACCA is the global body for professional accountants, supporting 131,500 members and 362,000 students throughout their careers, and providing services through a network of 82 offices and centres.

We aim to offer the first-choice qualifications to people of application, ability and ambition around the world who seek a rewarding career in accountancy, finance and management. ACCA works to achieve and promote the highest professional, ethical and governance standards and advance the public interest.

ACCA NATIONAL AWARDS

The combination of ACCA's work in improving the accountability and transparency of business and the success of the UK Awards in communicating these values to organisations has led a number of national ACCA offices to set up award schemes of their own. ACCA is now involved in reporting awards in more than 20 countries throughout Europe, Africa, North America and the Asia-Pacific region. ACCA award schemes are now established in Sri Lanka, Pakistan (in partnership with WWF), Malaysia, Singapore, Hong Kong, Australia and New Zealand, South Africa, and North America (in partnership with Ceres).

Launching award schemes in a number of countries around the world has helped raise the profile of corporate disclosure issues within those countries and among their national organisations. The ACCA awards serve to encourage non-reporters to publish information on their impacts and, ultimately, to help underline the business case for sustainable practices and development.

ACCOUNTING & SUSTAINABILITY E-NEWSLETTER

This publication, issued on a quarterly basis, provides a comprehensive guide to developments in accounting and sustainable development. The e-newsletter covers issues such as:

- management accounting, accounting for externalities and environmental finance
- environmental taxation and other legislation
- sustainability, environmental and social reporting
- third-party verification
- developments in standardisation, and
- socially responsible investment.

To receive e-mail notification of future issues, please register at www.accaglobal.com/sustainability

ACCOUNTING & CLIMATE CHANGE E-NEWSLETTER

This publication, which is new for 2009 and issued on a quarterly basis, provides a comprehensive guide to developments in relation to accounting and climate change. The e-newsletter covers issues such as:

- ACCA's own activities in the climate change arena
- climate change research
- carbon accounting and reporting
- climate change related legislation and changing regulatory requirements
- emissions trading schemes
- carbon markets and pricing
- government activities
- carbon reporting and assurance standards.

To receive e-mail notification of future issues, please register at www.accaglobal.com/climatechange

THE EUROPEAN SUSTAINABILITY REPORTING ASSOCIATION (ESRA)

1996 saw the launch of the European Environmental Reporting Awards, which were founded by ACCA and accountancy bodies from the Netherlands and Denmark.

These European Sustainability Reporting Awards were held for ten years, until 2006. In that decade a vast improvement was witnessed in both report numbers and quality of reporting. From 2006, the European partners were involved in a new project, focusing on sharing European reporting developments and best practice, from both a country-specific and regional perspective.

The results of this initiative from 2006, 2007 and 2008 can be viewed at www.sustainabilityreporting.eu

SOCIAL AND ENVIRONMENTAL COMMITTEE

ACCA's Social and Environmental Committee aims to bring together key players in the environmental and social fields to address relevant developments and issues concerning this aspect of accountancy.

www.accaglobal.com/sustainability

FÉDÉRATION DES EXPERTS COMPTABLES EUROPÉENS (THE EUROPEAN FEDERATION OF ACCOUNTANTS, FEE)

ACCA has been involved for many years in the environment- and sustainability-related work of FEE, together with representatives from other accountancy bodies across Europe. Work in this area includes promoting the role of the accountancy profession in, and stimulating debate on, sustainability accounting, reporting and auditing. It encourages pan-European studies and research programmes and disseminates their results, and represents the European accountancy profession at international level on environmental and social issues.

www.fee.be

ACCA SOCIAL AND ENVIRONMENTAL RESEARCH

A number of research projects have been funded by ACCA and these are listed in the *Research Publications Catalogue*. Issues researched include sustainability accounting in local government, social and environmental reporting, ethical investment, full cost accounting, social capital, and ecological footprint analysis.

www.accaglobal.com/research

About the CIPD



The Chartered Institute of Personnel and Development (CIPD) is Europe's largest professional body specialising in the field of HR. As a globally recognised brand and with over 133,000 members in 120 countries, we support and develop the HR experts responsible for the people who drive organisations.

Renowned as the creators of leading-edge research, we draw on the experiences and knowledge of the profession to provide solid benchmarks that can be used in the analysis of both current and emerging global trends in people management and development.

We work closely with the world's leading brands and renowned academics to deliver case studies, research papers, practical tools and insights. The results are regularly presented to audiences across the world at conferences and frequently referred to in the press.

The flexibility and expertise of our research team also means that we conduct research that is not only topical but also practical. This allows us to translate and embed our thinking into the products and services we offer.

Our members and customers see us not only as the leading authority, but also as the voice of the profession and a brand they can trust.

www.cipd.co.uk/research

TECH-TP-HCM